



A REPORT  
TO THE  
ARIZONA LEGISLATURE

Financial Audit Division

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Management Letter

# Pima County

Year Ended June 30, 2003

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**Debra K. Davenport**  
Auditor General

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**STATE OF ARIZONA  
OFFICE OF THE  
AUDITOR GENERAL**

DEBRA K. DAVENPORT, CPA  
AUDITOR GENERAL

WILLIAM THOMSON  
DEPUTY AUDITOR GENERAL

July 27, 2004

Board of Supervisors  
Pima County  
130 West Congress Street, 11th Floor  
Tucson, AZ 85701-1317

Members of the Board:

In planning and conducting our single audit of Pima County for the year ended June 30, 2003, we performed the following as required by *Government Auditing Standards* (GAS) and Office of Management and Budget (OMB) Circular A-133:

- Considered the County's internal controls over financial reporting,
- Tested its internal controls over major federal programs, and
- Tested its compliance with laws and regulations that could have a direct and material effect on its financial statements and major federal programs.

All audit findings that are required to be reported by GAS and OMB Circular A-133 have been included in the County's Single Audit Reporting Package for the year ended June 30, 2003. In addition, our audit disclosed internal control weaknesses and instances of noncompliance with laws and regulations that do not meet the reporting criteria. Management should correct these deficiencies to ensure that it fulfills its responsibility to establish and maintain adequate internal controls and comply with laws and regulations. Our recommendations are described in the accompanying summary.

In addition, as required by Arizona Revised Statutes §41-1279.21(A)(1), we reviewed the County's financial records to evaluate whether the County used Highway User Revenue Fund monies and any other dedicated state transportation monies solely for authorized transportation purposes. Our review to-date identified a portion of Pima County Transportation Department expenditures that were not for authorized transportation purposes, which is described in the accompanying summary as Recommendation 4. However, we have requested an opinion from the Arizona Attorney General about whether certain types of county transportation department expenditures are for transportation purposes authorized by the Constitution and state laws, but have not yet received a response to our request. Once we receive the opinion, we will complete our review and report any additional instances of noncompliance in a separate letter.

This letter is intended solely for the information of the Pima County Board of Supervisors and is not intended to be and should not be used by anyone other than the specified party. However, this letter is a matter of public record, and its distribution is not limited.

Should you have any questions concerning its contents, please let us know.

Sincerely,

Dennis L. Mattheisen, CPA  
Financial Audit Director

# TABLE OF CONTENTS

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Recommendation 1: The County needs better financial reporting procedures	1
Recommendation 2: The County needs to improve its capital assets reporting	2
Recommendation 3: The Public Fiduciary's Office should properly administer wards' assets	3
Recommendation 4: The County should ensure that state highway user revenues are spent according to state laws	4
County Response	

# The County needs better financial reporting procedures

The County is responsible for preparing an accurate and timely financial report to satisfy the audit requirements imposed by federal and state laws and regulations, grant contracts, and long-term debt covenants. However, the County provided auditors with inaccurate financial statements and various supporting schedules 1 to 2 weeks after agreed-upon completion dates. As a result, auditors had to spend significant time and effort assisting the County so that it could issue an accurate and complete financial report by the Government Finance Officers Association certification deadline. Auditors recommended many significant adjustments to financial statement amounts as well as many corrections to note disclosures and other report schedules.

To help ensure that the County's financial report is prepared accurately and issued by the agreed-upon dates, it should establish procedures to:

- Ensure that financial statement amounts agree to supporting schedules. For example, schedules prepared to calculate compensated absences payable or depreciation expense should agree to reported balances.
- Analyze amounts on the governmental funds reconciliation statements and make sure that they are consistent with the amounts reported on the government-wide and fund financial statements.
- Verify that amounts reported within various sections of the financial report agree. For example, transfers in and out should be equal and amounts in the notes to financial statements and management's discussion and analysis should agree to the corresponding financial statement amounts.
- Develop and use a checklist of accounting and reporting requirements to help ensure that financial statements are properly presented in accordance with authoritative pronouncements.
- Have an employee who did not prepare the financial report review it to help ensure that it is appropriately formatted for publication and that the column and row totals are mathematically accurate.

# The County needs to improve its capital assets reporting

Capital assets, net of accumulated depreciation, represent more than 75 percent of the County's total assets. Therefore, the County should safeguard these assets and accurately report them to its creditors, the public, and other interested parties. To accomplish this, the County should maintain a reliable capital assets system and follow procedures that accurately identify capital assets purchases, and list and reconcile associated costs and depreciation. However, the County had not established an adequate system or internal control policies and procedures that would ensure its capital assets were properly reported. For example, the County capitalized over \$11.5 million of noncapital purchases, misclassified land that cost \$12.9 million as construction in progress, and overstated construction in progress by more than \$37 million. Further, due to problems with the current capital assets system, the County could not determine accurate depreciation amounts and could not reconcile capital expenditures recorded in the financial accounting system to additions in the capital assets system.

The following procedures can help the County accurately record its capital assets in its accounting records and report those assets in its financial statements:

- Develop written internal control policies and procedures for county departments that explain how to accurately classify and record capital purchases in the accounting records.
- Establish procedures that require employees to perform a detailed review of capital purchases that are recorded in the accounting records.
- Develop a capital assets system that accurately calculates depreciation and provides a listing of current-year additions that can be reconciled to capital expenditures recorded in the financial accounting system.

# The Public Fiduciary's Office should properly administer wards' assets

State statutes require counties to provide the monies necessary to operate a public fiduciary's office and require fiduciaries to exercise extreme care and diligence when making decisions on behalf of wards. Wards are individuals assigned by the court to a fiduciary when the court finds the individuals are unable to handle their own affairs and when there is no one else qualified or willing to do so.

The Pima County Public Fiduciary's Office did not always follow state statutes because it did not distribute interest earned on the wards' deposits in a shared checking account to the wards' balances. Instead, the Office entered into a bank agreement through which the bank paid over \$21,000 of the Office's fiscal year 2003 operating costs with credits earned from the wards' deposits. In addition, the Office's banking agreement did not specify earnings rates and minimum balances, and the Office did not compare its bank's costs and benefits with those of other banks. Therefore, the Office could not ensure that the wards received the highest possible return on their deposits.

The Public Fiduciary's Office must exercise extreme care and diligence and properly distribute and report the wards' interest income. At a minimum, the Office should:

- Ensure that it selects the bank that will provide the wards the highest possible returns by comparing banks' interest rates, banking fees, and minimum deposit requirements, before entering into a banking agreement. Also, the Office should ensure that the written banking agreement clearly stipulates such information and is signed and approved by the appropriate level of county management.
- Distribute interest earned on the wards' shared checking account to the wards balances at least quarterly based on their average balances.
- Budget its expenditures so that the monies provided by the County are adequate to operate the Office as required by Arizona Revised Statutes (A.R.S.) §14-5601. If the Office finds it necessary to charge the wards reasonable service fees as allowed by A.R.S. §14-5604, the Office must obtain court approval for all costs charged to a ward, report the charges to the court, and deposit any fees collected into the County's General Fund.
- Ensure that all office operating costs are paid from the County's General Fund after following the County's purchasing policies and procedures rather than paid by a banking institution.

## The County should ensure that state highway user revenues are spent according to state laws

Each year, the state distributes highway user revenue fund (HURF) monies and a portion of the vehicle license tax (VLT) monies to the County and mandates that the County use these monies solely for highway and street purposes. During the fiscal year, the County Transportation Department received over \$48 million in HURF and restricted VLT monies, more than 90 percent of the Department's revenues. Although the Department used most of these monies to help finance highway and street construction, repairs, and maintenance and to pay principal and interest on transportation bonds, it also used them to pay costs that were not for highway and street purposes. Auditors noted that the County Transportation Department spent approximately \$4.6 million of HURF and restricted VLT monies to finance public transportation costs such as City of Tucson bus service, rural transit services, and special needs transportation services.

The County should develop written policies that clearly define the allowable uses of HURF and restricted VLT monies and ensure that its transportation department follows these policies. In addition, the County should review and approve the proposed uses of these monies to help ensure that they are spent in accordance with the Arizona Constitution, Article 9, §14. Finally, the County should allocate an additional \$4.6 million of local revenues for highway and street purposes to replenish the monies it spent inappropriately.



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Carol M. Bonchalk, Director

July 20, 2004

Ms. Debbie Davenport  
Auditor General  
2910 N 44th St., Suite 410  
Phoenix, AZ 85018

Dear Ms. Davenport:

The following are Pima County's response to the Management Letter comments for Fiscal Year 2003/2004. If you have any questions, please feel free to call.

Sincerely,

Carol M. Bonchalk, Director  
Finance Department

CMB:phs

Attachment

## **The County needs better financial reporting procedures**

The County has reviewed the audited adjustments that have generated a significant portion of this finding. Based on this review, we found that almost 60% of auditor recommended adjustments to the financial statements were a result of our capital asset reporting system. These specific adjustments affected several financial statements, including the notes to the financial statements, the management's discussion and analysis and the reconciliation statements for the governmental funds. The County addresses the weaknesses of its capital asset reporting system in the response below.

The County agrees significant improvements are needed in the financial reporting procedures, including the accuracy, manner and timing of when the financial statements, supporting schedules, reconciliation statements and notes to the financials are provided for audit. An employee not involved with the audit will be assigned to review the financial statements and related documents for accuracy and consistency prior to distribution to the Auditor General.

Our focus for the fiscal year 2003/2004 audit will be to provide all requests from the auditors on a timely basis, while maintaining procedural controls over the flow of information between the County and its auditors. The flow and timing of communication between the County and its auditors will be monitored to ensure recommended adjustments are directed to appropriate management for action.

## **The County needs to improve its capital asset reporting**

The County's implementation of Government Accounting Standards Board Statement No. 34 (GASB 34) in the prior year (FY 2001/02) has identified significant weaknesses in our financial system for reporting capital assets. One of the new reporting requirements of GASB 34 was the application of depreciation expense to governmental funds – a requirement our current asset reporting system is not able to capture and report from without significant manual adjustments. These manual adjustments are prone to error and have contributed directly to this finding.

An asset management software has been purchased by the County and implementation has begun. We are expecting the new asset management system to eliminate the intensively manual effort found in the current system. Concurrently, the County is evaluating and aggressively modifying the flow of information to allow for an accurate reporting of our capital assets, while also creating new efficiencies in our business practices.

## **The Public Fiduciary's Office should properly administer wards' assets**

The Public Fiduciary's Office maintains policies and procedures to ensure that the interests of its wards are protected and maintained. The County has reviewed the finding issued by its auditors and will undertake the following:

- a review and revision of the banking agreement to ensure compliance with applicable laws, rules and policies.
- an analysis of the budget, current operating costs of the Office and revenues including charges for services and interest earnings.
- an analysis of the cost/benefit associated with the distribution of interest earned on pooled funds.

## **The County should ensure that state highway user revenues are spent according to state laws**

Pima County disagrees with the position taken in this audit regarding constitutional restrictions on Pima County's use of unrestricted VLT funds received pursuant to §28-5808 (A) (2) (b), deposited in the County's Transportation fund. We further believe that our transportation program expenditures of HURF funds and unrestricted VLT funds have been in full compliance with all applicable statutes and regulations.